

## HOUSE OF REPRESENTATIVES STAFF ANALYSIS

**BILL #:** HB 339 Motor Vehicle Service Agreement Companies

**SPONSOR(S):** White

**TIED BILLS:** **IDEN./SIM. BILLS:** SB 794

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Insurance & Banking Subcommittee		Lloyd	Luczynski
2) Commerce Committee			

### SUMMARY ANALYSIS

Motor vehicle service agreement companies are one type of warranty association and are governed by the provisions in part I of ch. 634, F.S. Motor vehicle service agreements generally provide vehicle owners with protection when the manufacturer's warranty expires. Warranty associations are regulated by the Office of Insurance Regulation (OIR). The OIR's regulatory authority concerning warranty associations includes approval of forms, investigation of complaints, and monitoring of reserve requirements, among other duties. However, the OIR is not required to approve rates for warranties. Among other requirements, motor vehicle service agreement companies may meet statutory reserve requirements by purchasing contractual liability insurance from an admitted insurer.

Motor vehicle service agreements indemnify the agreement holder against loss caused by failure of any mechanical or other component part, or any mechanical or other component part of the motor vehicle that does not function as it was originally intended. The term "motor vehicle service agreement" also includes any contract that provides: for coverage which is issued in conjunction with an additive product applied to the motor vehicle that is the subject of such agreement; for payment of vehicle protection expenses (such as meeting applicable deductibles and providing for temporary replacement vehicle rental expenses); and for the payment for paintless dent-removal services.

A risk retention group is a corporation or limited liability association whose primary purpose is to share any or all of the liabilities of the members of the group. If they are organized under the law of any state or district of the United States, they may transact business in Florida. They may not exclude businesses from membership solely for competitive advantage. Membership in the group is limited to those engaged in business or activities that result in similar or related liabilities because of their similar, related or common business conditions. These groups may only be owned by their members or organizations owned by their members.

Risk retention groups can only insure certain risks. They are limited to liability insurance and reinsurance of other risk retention groups that share the same common interests required to form a group. The term "risk retention group" must be included in the group's name and they do not benefit from Florida's insurance insolvency guaranty funds. There are 108 risk retention groups active in Florida.

The bill increases the minimum surplus to policyholders applicable to insurers providing coverage for contractual liabilities of a motor vehicle service agreement company from \$4,000,000 to \$15,000,000. It allows service agreement companies to meet their reserving requirements by participating in a risk retention group if the group covers 100 percent of the claims exposure and maintains a surplus to policyholders minimum of \$15,000,000. Lastly, it allows companies that offer vehicle protection expenses to meet their reserve requirements related to contractual liability for vehicle protection expense claims through risk retention groups, in addition to the purchase of insurance, and removes a prohibition on them utilizing an affiliated insurer to meet their reserve requirements.

The bill does not appear to have a fiscal impact on state or local government.

The bill has an effective date of July 1, 2017.

## FULL ANALYSIS

### I. SUBSTANTIVE ANALYSIS

#### A. EFFECT OF PROPOSED CHANGES:

##### **Motor Vehicle Service Agreement Companies**

Motor vehicle service agreement companies are one type of warranty association and are governed by the provisions in part I, ch. 634, F.S. Motor vehicle service agreements generally provide vehicle owners with protection when the manufacturer's warranty expires. While a warranty is not considered a traditional insurance product, it protects purchasers from future risks and associated costs. In Florida, warranty associations are regulated by the Office of Insurance Regulation (OIR). The OIR's regulatory authority concerning warranty associations includes approval of forms, investigation of complaints, and monitoring of reserve requirements, among other duties. However, the OIR is not required to approve rates for warranties.

Motor vehicle service agreements indemnify the agreement holder against loss caused by failure of any mechanical or other component part, or any mechanical or other component part of the motor vehicle that does not function as it was originally intended. The term "motor vehicle service agreement" also includes any contract that provides: for coverage which is issued in conjunction with an additive product applied to the motor vehicle that is the subject of such agreement; for payment of vehicle protection expenses (such as meeting applicable deductibles and providing for temporary replacement vehicle rental expenses); and for the payment for paintless dent-removal services.<sup>1</sup>

These companies are required to be licensed by the OIR prior to conducting business in Florida.<sup>2</sup> A company must meet the following conditions to qualify for licensure:<sup>3</sup>

- Be a solvent corporation,
- Prove to OIR that the management of the company is competent and trustworthy and can successfully and lawfully manage the company,
- Deposit \$200,000 with the Department of Financial Services (DFS),<sup>4</sup>
- Have and maintain minimum net assets of at least \$500,000, which must be kept in the United States,
- Keep and maintain an unearned premium reserve of at least 50 percent of the unearned gross written premium of each service agreement amortized pro rata over the life of the agreement, kept in a 10 to 1 ratio of gross written premium in force to net assets<sup>5</sup> (15% of this reserve must be deposited with the DFS),
  - This reserve is not required if the service agreement company holds a contractual liability policy and meets the following criteria:
    - The policy covers 100 percent of the claim exposure and is with an admitted insurer,
    - If the service agreement company fails to meet its contractual obligations, the insurer<sup>6</sup> is bound to cover all claims and refunds on agreements issued during

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<sup>1</sup> s. 634.011(8), F.S.

<sup>2</sup> s. 634.031, F.S. The unauthorized transaction of motor vehicle service agreements is a first degree misdemeanor punishable by up to one year in jail and a \$1,000 fine. s. 634.031(7), F.S.

<sup>3</sup> s. 634.041, F.S.

<sup>4</sup> s. 634.052, F.S. If the company maintains less than \$750,000 in unearned gross premium, the deposit may be lowered to \$100,000. Also, the deposit may be lowered to no less than \$100,000 after the first year of business upon application to the DFS for a release of a portion of the deposit. For good cause shown after notice and a hearing, the OIR may require the deposit to be increased to no more than \$500,000 to protect the company's customers and creditors. The deposit must be in the form of the various securities specified in s. 625.52, F.S.

<sup>5</sup> This ratio only applies to the direct written premiums covered by the reserve, i.e., that are retained and not covered by contractual liability insurance held by the service agreement company. s. 634.041(8)(a)2., F.S.

<sup>6</sup> Contractual liability insurance is casualty insurance. s. 624.605(1)(b), F.S. Casualty insurers are required to initially have at least \$5,000,000 in surplus as to policyholders and subsequently must maintain \$4,000,000 in surplus as to policy holders. ss. 624.407 and 624.408, F.S.

- the policy period, including those agreements that the company has yet to pay premium on,
  - If the service agreement is being fulfilled by the insurer and the company cancels the agreement, the insurer must issue the required pro rata refund (and representatives or agents must refund the commissions, pro rata),
  - There is a 90 day cancellation, termination, or non-renewal notice to OIR by the insurer, and
  - The company provides claim statistics to OIR.
- The service agreement company must be able to identify which allowed reserve requirement is being used to back each agreement. However, a company with at least \$10,000,000 in assets and a audited actuarial statement on file with OIR is granted authority to manage blocks of new agreements under either of the two allowed forms of reserving, i.e., the 50 percent reserve or contractual liability insurance substitute,
- It must file, under oath of two executive officers, any information requested in writing by OIR regarding its transactions and affairs, and
- Limitations on reserve requirements apply to service agreement companies that provide vehicle protection expenses through their agreements, including a prohibition on purchasing insurance from an affiliated insurer.<sup>7</sup>

The OIR is prohibited from licensing a company if it has violated any requirement of part I of ch. 634, F.S., or any rules interpreting and implementing that part within the previous three years. There are 89 motor vehicle service agreement companies active in Florida.<sup>8</sup>

## Risk Retention Groups

Risk retention groups are authorized under state and federal law.<sup>9</sup> Except for requirements related to oversight of the formation and operations of the group, the regulation of these groups is preempted by federal law.<sup>10</sup>

A risk retention group is a corporation or limited liability association whose primary purpose is to share any or all of the liabilities of the members of the group. If they are organized under the law of any state or district of the United States, they may transact business in Florida.<sup>11</sup> They may not exclude businesses from membership solely for competitive advantage. The group must be solely owned by either:

- its members who receive insurance from the group, or
- by an organization whose members are the members of the group; however, the owning organization must be owned by those making up and receiving insurance from the group.

The group members must be engaged in business or activities that result in similar or related liabilities because of their similar, related or common business conditions.

Risk retention groups can only insure certain risks. They are limited to liability insurance and reinsurance of other risk retention groups that share the same common interests required to form a group. The term “risk retention group” must be included in the group’s name. None of Florida’s

<sup>7</sup> The service agreement company can use an affiliated insurer, if the insurer had issued them a policy prior to January 1, 2002. s. 634.041(11)(a), F.S.

<sup>8</sup> FLORIDA OFFICE OF INSURANCE REGULATION, ACTIVE COMPANY SEARCH, <http://www.floir.com/CompanySearch/>, Select “Motor Vehicle Service Agreement Company” under “Company Type” (last visited Feb. 17, 2017).

<sup>9</sup> 15 U.S.C. §§ 3901, et seq. (2016), and part XIX of ch. 627, F.S.

<sup>10</sup> 15 U.S.C. §3902 (2016). Rule 69-O-200.006, F.A.C., requires insurers writing contractual liability insurance to obtain a certificate of authority from OIR prior to doing so. Since risk retention groups from outside of Florida are not issued certificates of authority, the OIR asserts that they cannot offer contractual liability insurance in the state. Florida Office of Insurance Regulation, Agency Analysis of 2017 House Bill 339, p. 5 (Feb. 1, 2017). This rule may conflict with federal preemption regarding risk retention groups and would be resolved by the bill.

<sup>11</sup> Certain risk retention groups organized in Bermuda or the Cayman Islands prior to January 1, 1985, may also transact business in Florida. s. 627.942(9)(c)2., F.S.

insurance insolvency guaranty funds are available for risk retention group insolvencies. There are 108 risk retention groups active in Florida.<sup>12</sup>

By forming or joining a risk retention group, a prospective member, such as a motor vehicle service agreement company, can take advantage of economic opportunities consistent with self-insurance. They may be able to save money by controlling overhead costs and profits that cannot be avoided through the purchase of insurance. They maintain or participate in the control of assets and investments dedicated to the reserves that will fund claims exposure. The availability of participation in risk retention groups provide business with another option to compete in the market and take advantage of economic opportunities.

### **Effect of the Bill**

The bill:

- Increases the minimum surplus to policyholders that is applicable to any insurer providing coverage for contractual liabilities of a motor vehicle service agreement company. The minimum surplus as to policyholders is increased from \$4,000,000 to \$15,000,000.
- Allows service agreement companies to meet their reserving requirements by participating in a risk retention group, if the group:
  - Covers 100 percent of the claims exposure of the company, and
  - Maintains a surplus to policyholders minimum of \$15,000,000.
- Regarding service agreement companies that offer vehicle protection expenses in their agreements, the bill:
  - Allows them to meet their reserve requirements related to contractual liability for vehicle protection expense claims through risk retention groups, rather than exclusively through the purchase of insurance, and
  - Removes a prohibition on them utilizing an affiliated insurer to meet their reserve requirements.

### **B. SECTION DIRECTORY:**

**Section 1.** Amends s. 634.041, F.S., relating to qualifications for licensure.

**Section 2.** Provides an effective date of July 1, 2017.

## **II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT**

### **A. FISCAL IMPACT ON STATE GOVERNMENT:**

#### **1. Revenues:**

None.

#### **2. Expenditures:**

None.

### **B. FISCAL IMPACT ON LOCAL GOVERNMENTS:**

#### **1. Revenues:**

None.

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<sup>12</sup> FLORIDA OFFICE OF INSURANCE REGULATION, ACTIVE COMPANY SEARCH, <http://www.floir.com/CompanySearch/>, Select “Risk Retention Group” under “Company Type” (last visited Feb. 17, 2017).

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

The bill may increase the amount of and options related to contractual liability coverage of motor vehicle service agreements.

D. FISCAL COMMENTS:

None.

### III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

Not applicable. The bill does not appear to affect county or municipal governments.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

None provided by the bill.

C. DRAFTING ISSUES OR OTHER COMMENTS:

Lines 20 through 29 of the bill allow motor vehicle service agreement companies to insure their reserve obligations through the purchase of contractual liability insurance from either an insurer or a risk retention group. However, one does not purchase from a risk retention group; rather, one joins as a member of the group and obtains coverage through participating in group membership. An amendment to this provision would more accurately describe the allowed methods of complying with the law.

In its bill analysis, the Office of Insurance Regulation points out that the term “surplus as to policyholders” in current law should be “surplus as regards policyholders.”<sup>13</sup>

### IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES

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<sup>13</sup> Florida Office of Insurance Regulation, Agency Analysis of 2017 House Bill 339, p. 5 (Feb. 1, 2017).